



# Walmart Inc. (WMT)

Updated August 28<sup>th</sup>, 2019 by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$112	<b>5 Year CAGR Estimate:</b>	-0.6%	<b>Volatility Percentile:</b>	28.9%
<b>Fair Value Price:</b>	\$74	<b>5 Year Growth Estimate:</b>	5.5%	<b>Momentum Percentile:</b>	80.7%
<b>% Fair Value:</b>	151%	<b>5 Year Valuation Multiple Estimate:</b>	-8.0%	<b>Growth Percentile:</b>	52.2%
<b>Dividend Yield:</b>	1.9%	<b>5 Year Price Target</b>	\$97	<b>Valuation Percentile:</b>	6.7%
<b>Dividend Risk Score:</b>	A	<b>Retirement Suitability Score:</b>	B	<b>Total Return Percentile:</b>	4.5%

## Overview & Current Events

Walmart traces its roots back to 1945 when Sam Walton opened his first discount store. The company has since grown into the largest retailer in the world, serving 270 million customers each week. Revenue will be well in excess of \$500 billion this year and the stock trades with a market capitalization of \$321 billion.

Walmart reported Q2 earnings on 8/15/19 and results were strong once again, leading us to boost our earnings-per-share estimate for this year. Total revenue was up 1.8% to \$130 billion in Q2. On a currency-neutral basis, revenue would have risen 2.9% to \$132 billion.

The company reported its 20<sup>th</sup> consecutive quarter of growth in the US, as comparable sales rose on a two-year stacked basis by 7.3%. eCommerce growth was 37% in Q2, driven by continued adoption of online grocery sales. However, segment operating income was up only 4% as the company continues to struggle with margins in the face of heavy growth investment spending.

Sam's Club comparable sales rose 1.2% and eCommerce sales rose 35%. Walmart indicated reduced tobacco sales negatively impacted comparable sales by 300bps.

The international segment saw revenue of \$29 billion a decline of 1.1%. On a currency-neutral basis, sales would have been up 3.3%. Mexico and China were sources of strength, offset somewhat by the UK and Canada.

Total operating income was down 2.9% on a reported basis, or 2.4% on a constant currency basis. Earnings-per-share were essentially flat in Q2 at \$1.27. We've boosted our estimate for earnings-per-share to \$4.95 following the Q2 report given that sales continue to come in stronger than expected. In addition, the company updated its guidance to essentially flat, versus prior guidance of a slight decline in earnings-per-share year-over-year.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$3.66	\$4.07	\$4.55	\$5.02	\$5.11	\$5.07	\$4.57	\$4.32	\$4.42	\$4.91	<b>\$4.95</b>	<b>\$6.47</b>
<b>DPS</b>	\$1.09	\$1.21	\$1.46	\$1.59	\$1.88	\$1.92	\$1.96	\$2.00	\$2.04	\$2.08	<b>\$2.12</b>	<b>\$2.71</b>
<b>Shares<sup>1</sup></b>	3,786	3,516	3,418	3,314	3,233	3,228	3,162	3,048	2,952	2,914	<b>2,860</b>	<b>2,620</b>

The largest concern for Walmart is operating margins, as gross margins have remained flat while operating expenses have risen, something we've seen for a few quarters now, Q2 included. This is the product of Walmart's focus on building out its online business as well as integrating its acquisitions, both of which are expensive endeavors. Q2's operating income showed the weakness of the company's margins once again, even while revenue is rising.

Looking forward, we are forecasting 5.5% annual earnings growth for the next five years as Walmart continues to work through its margin issues. The company continues to buy back stock as well. We see low single-digit sales growth each year, with its e-commerce business being the primary driver of top line growth. That combination should be good enough to create mid-single-digit growth without the benefit of margin expansion. We continue to be bullish on

<sup>1</sup> Share count in millions

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Walmart's ability to grow revenue, but its margins are suffering as a result. Presumably, margins will bottom out and perhaps we are seeing the first signs of that, but for now, our base case is slightly lower margins.

## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	13.9	13.1	12.4	13.5	14.9	15.4	15.5	16.2	18.9	18.8	22.7	15.0
Avg. Yld.	2.1%	2.3%	2.7%	2.3%	2.5%	2.5%	2.8%	2.9%	2.1%	2.3%	1.9%	2.8%

Walmart's valuation is currently at its highest level of the past decade. Investors continue to bet heavily on the future of the eCommerce business, but it has made the quite stock expensive. We are forecasting the price-to-earnings multiple to fall to 15, creating a high single-digit annual headwind on a total return basis as a result of the revaluation of the stock. The yield is down to 1.9% thanks to the higher valuation, at the lower end of its historical range. We expect the yield to rise in the coming years back towards the upper-2% range, commensurate with its historical norms.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	28%	30%	30%	33%	32%	37%	38%	43%	46%	42%	43%	42%

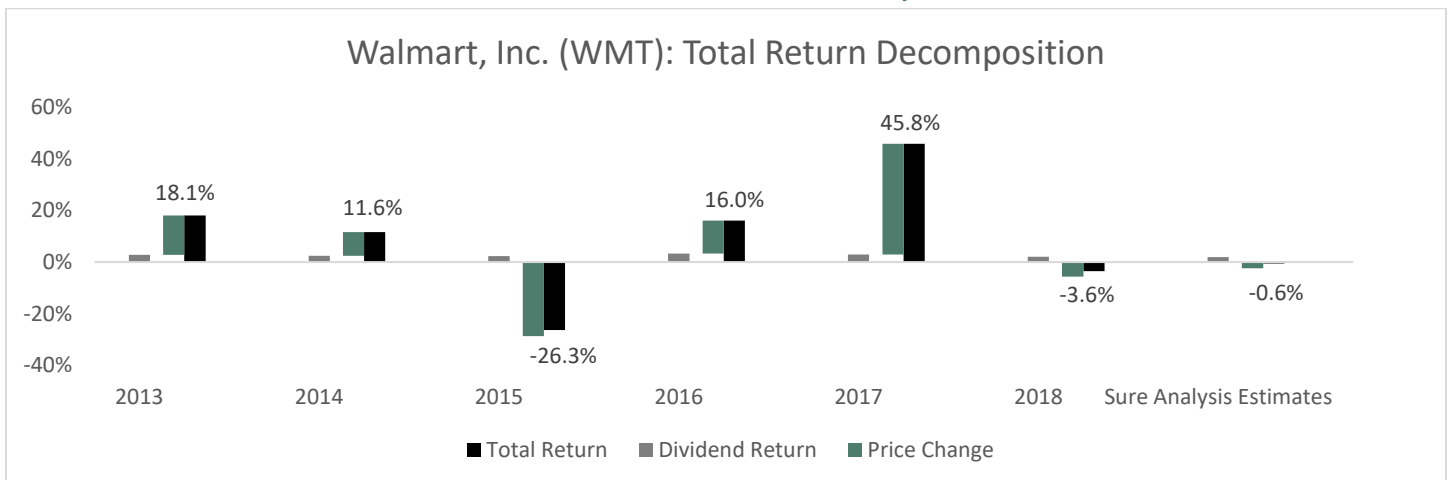
The company's payout ratio is quite low around 40% of earnings, making for a conservative dividend policy. The dividend should be safe, even if a strong recession strikes.

Walmart's competitive advantage is in its enormous size as it can buy and ship product at scales no other company can rival. This allows it to operate with low prices to consumers and as more than half of its revenue comes from groceries, its recession performance is excellent. The company managed to increase earnings steadily during and after the Great Recession. Hard economic conditions tend to send consumers on the margins to Walmart, which is also an advantage.

## Final Thoughts & Recommendation

Overall, Walmart looks overvalued as it continues to trade at a significant premium to our estimate of fair value. We are forecasting total five-year annual returns of just -0.6%, as the yield has come down and the valuation has risen, both attributable to a recent rally in the share price. Walmart is a safe, defensive stock in times of economic hardship, but growth is going to be limited as it works through its margin issues and a stock price that is well in excess of fair value. Given low projected total returns, the stock continues to earn a sell recommendation at current prices.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Revenue (\$B)</b>	408.09	421.85	446.5	468.65	476.3	485.65	482.13	485.87	500.3	514.41
<b>Gross Profit (\$B)</b>	103.98	106.90	111.5	116.35	118.2	120.57	121.15	124.62	127.0	129.10
<b>Gross Margin</b>	25.5%	25.3%	25.0%	24.8%	24.8%	24.8%	25.1%	25.6%	25.4%	25.1%
<b>SG&amp;A Exp. (\$B)</b>	79.98	81.36	85.03	88.63	91.35	93.42	97.04	101.85	106.5	107.15
<b>D&amp;A Exp.</b>	7157	7641	8106	8478	8870	9173	9454	10080	10529	10678
<b>Operating Profit</b>	24002	25542	26491	27725	26872	27147	24105	22764	20437	21957
<b>Op. Margin</b>	5.9%	6.1%	5.9%	5.9%	5.6%	5.6%	5.0%	4.7%	4.1%	4.3%
<b>Net Profit</b>	14370	16389	15699	16999	16022	16363	14694	13643	9862	6670
<b>Net Margin</b>	3.5%	3.9%	3.5%	3.6%	3.4%	3.4%	3.0%	2.8%	2.0%	1.3%
<b>Free Cash Flow</b>	14065	10944	10745	12693	10142	16390	16075	21054	18286	17409
<b>Income Tax</b>	7156	7579	7924	7958	8105	7985	6558	6204	4600	4281

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets (\$B)</b>	170.41	180.78	193.41	203.11	204.75	203.49	199.58	198.83	204.52	219.30
<b>Cash &amp; Equivalents</b>	7907	7395	6550	7781	7281	9135	8705	6867	6756	7722
<b>Acc. Receivable</b>	N/A	5089	5937	6768	6677	6778	5624	5835	5614	6283
<b>Inventories</b>	32713	36437	40714	43803	44858	45141	44469	43046	43783	44269
<b>Goodwill &amp; Int.</b>	16126	16763	20651	20497	19510	18102	16695	17037	18242	31181
<b>Total Liab. (\$B)</b>	97.45	109.54	117.65	121.37	123.41	117.55	115.97	118.29	123.70	139.66
<b>Accounts Payable</b>	30451	33676	36608	38080	37415	38410	38487	41433	46092	47060
<b>Long-Term Debt</b>	37804	46378	50092	50786	53544	47272	43667	39370	39040	50621
<b>Total Equity</b>	70468	68542	71315	76343	76255	81394	80546	77798	77869	72496
<b>D/E Ratio</b>	0.54	0.68	0.70	0.67	0.70	0.58	0.54	0.51	0.50	0.70

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	8.6%	9.3%	8.4%	8.6%	7.9%	8.0%	7.3%	6.8%	4.9%	3.1%
<b>Return on Equity</b>	21.2%	23.6%	22.5%	23.0%	21.0%	20.8%	18.1%	17.2%	12.7%	8.9%
<b>ROIC</b>	13.3%	14.4%	12.9%	13.2%	12.0%	12.2%	11.3%	11.0%	8.2%	5.3%
<b>Shares Out.</b>	3,786	3,516	3,418	3,314	3,233	3,228	3,162	3,048	2,952	2,914
<b>Revenue/Share</b>	105.26	114.95	128.53	138.29	145.08	149.75	149.87	156.13	166.23	174.67
<b>FCF/Share</b>	3.63	2.98	3.09	3.75	3.09	5.05	5.00	6.77	6.08	5.91

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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